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IN THE UNITED STATES DISTRICT COURT FOR THE  
NORTHERN DISTRICT OF ILLINOIS  
CHICAGO DIVISION

MICHAEL W. DOBBINS  
CLERK, U.S. DISTRICT COURT

UNITED STATES OF AMERICA,

Plaintiff,

v.

CARMELO ZANFEI; WILLIAM P. CROUSE,  
JR.; PARADIGM SOLUTIONS GROUP, LLC;  
and SUPERIOR SOLUTIONS GROUP, INC.

Defendants.

Civil No.

04C 2703

Judge: JUDGE NORDBERG

MAGISTRATE JUDGE DENLOW

COMPLAINT FOR PERMANENT INJUNCTION  
AND OTHER RELIEF

The plaintiff, the United States of America, alleges as follows:

1. The United States brings this complaint pursuant to §§ 7402(a) and 7408 of the Internal Revenue Code (26 U.S.C.) (IRC) to restrain and enjoin the defendants from:
  - a. engaging in any activity subject to penalty under IRC § 6700, including organizing or selling a plan or arrangement and, in connection with that activity, making a statement regarding the excludability of income or securing of any other tax benefit that they know or have reason to know is false or fraudulent as to any material matter;
  - b. engaging in any other activity subject to penalty under IRC §§ 6700;
  - c. engaging in other, similar conduct that unlawfully interferes with the proper administration and enforcement of the internal revenue laws.

### **Parties**

2. The plaintiff is the United States of America.

3. The defendant Carmelo Zanfei resides at 318 Royal Oak Court, Steger, Illinois, 60475.

He regularly conducted business from offices in Calumet City and Chicago Heights, Illinois. He is within this Court's jurisdiction.

4. The defendant William P. Crouse, Jr., resides at 4181 Waterbrook Way, Greenwood, Indiana, 46143-9307. He regularly conducted business from offices in Calumet City and Chicago Heights, Illinois. He is within this Court's jurisdiction.

5. The defendant Paradigm Solutions Group, LLC (PSG) is a limited liability company formed in the state of Delaware. Its registered agent is Registered Agents, Ltd, Ste 606, 1220 N. Market Street, Wilmington, Delaware. PSG carries on systematic business activities within the state of Illinois. It is subject to this Court's jurisdiction.

6. Defendants Zanfei and Crouse are officers and managers of PSG.

7. The defendant Superior Solutions Group, Inc., [SSG] is a Nevada Corporation with a business address of 211 N. Buffalo Drive, Suite A, Las Vegas, Nevada, 89145. SSG carries on systematic business activities within the state of Illinois and is subject to this Court's jurisdiction. The registered agent for SSG is Christopher Rhodes, 5172 E. 65th St., Suite 105, Indianapolis, Indiana, 46220.

8. Defendants Zanfei and Crouse are the sole shareholders of SSG.

### **Jurisdiction and Venue**

9. This Court has jurisdiction over this action under 28 U.S.C. §§ 1340 and 1345 and §§ 7402(a) and 7408 of the IRC.

10. This action has been requested by the Acting Chief Counsel of the Internal Revenue Service, a delegate of the Secretary of the Treasury, and commenced at the direction of a delegate of the Attorney General of the United States, pursuant to the provisions of IRC §§ 7402 and 7408.

11. Venue is proper in this Court pursuant to 28 U.S.C. § 1391.

**Defendants' Activities**

12. Defendants Zanfei and Crouse, through various entities, including The Redwood Group, LLC; The Redwood Group, Inc., TRG Marketing, LLC, and defendants SSG and PSG, are organizing and marketing abusive tax schemes to help customers unlawfully avoid federal income and employment taxes. The schemes are shelters, plans, or arrangements within the meaning of IRC § 6700.

13. Defendants sell schemes called the Health Incentive Plan (HI Plan) and the HealthIER Plan to employers. The schemes are designed to cause the customers to unlawfully underreport wages paid on their quarterly federal employment tax returns and on IRS Form W-2 wage statements given annually to the customers' employees. This in turn results in the employer-customers underreporting and underpaying their federal employment taxes and in the employees underreporting and underpaying their federal income taxes. This underreporting also results in employers understating wages to the Social Security Administration. The underreporting arises from unlawfully excluding from wages certain amounts that the employer-customers pay to employees as purported accident and health insurance premiums and purported reimbursements of employees' medical expenses. Zanfei began selling the HI Plan in January of

2000. Crouse started selling the HI Plan in Spring 2000. Defendants began promoting the HealthIER Plan in 2003.

14. The HI Plan causes the defendants' customer-employers to unlawfully underreport wages paid on federal employment tax returns and W-2 forms by reducing reported wages twice for employer-paid health insurance premiums, using the following steps:

**Step 1:** The customer-employers pay health insurance premiums for employees and correctly exclude those amounts from reported wages on the customer-employers' federal employment tax returns and the W-2 forms issued to employees.

**Step 2:** In addition to paying employees' health insurance premiums directly, the defendants' customer-employer also purportedly "reimburses" the employees in an amount approximately equal to the amount of health insurance premiums paid by the employer. These "reimbursements," which under the scheme are excluded from reported wages, are in fact nothing of the sort. They are simply wages disguised as reimbursements in order to reduce reported wages paid on the employer's federal employment tax returns.

IRC § 105(b) excludes under specified circumstances employer reimbursements of employees' medical care expenses from gross income and wages for employment taxes. But amounts paid under the defendants' HI Plan are not "reimbursements;" therefore there is no lawful basis for the exclusion.

15. The HealthIER Plan unlawfully causes the defendants' customer-employers to underreport and underpay federal employment taxes by excluding from wages reported on employment tax returns amounts paid to employees as medical expense "reimbursements" for

expenses that have not been incurred. The HealthIER Plan uses the following steps to implement this fraudulent scheme:

**Step 1:** As with the HI Plan, under the HealthIER Plan the defendants' customer-employers paid accident and health insurance premiums on behalf of employees, and properly excluded those payments from reported wages on their federal employment tax returns.

**Step 2:** But in addition, under the HealthIER Plan the defendants' customer-employers set up a stand-alone medical reimbursement plan. The HealthIER Plan calls for the customer-employer to automatically make "advance reimbursements" of employees' medical expenses. These advance reimbursements are made regardless of whether employees have actually incurred medical expenses. Stated simply, the so-called reimbursements are not reimbursements at all—they are wages disguised as reimbursements, to allow the customer-employers to fraudulently underreport wages paid on their federal employment tax returns and on W-2 wage statements. This results in the customer-employers under-reporting and underpaying their employment taxes and results in the employees under-reporting and underpaying their federal income and social security taxes.

16. Defendants charge their customer-employers a fee of \$10 per employee to sign up for the HealthIER Plan. Defendants also charge a fee of \$20 per month per employee for the HealthIER Plan scheme. Although it is the customer-employers who contract with the defendants for the scheme, the monthly fees are taken out of the paychecks of customers' employees, resulting in the employees paying for their employers' participation in the scheme.

17. Under defendants' schemes, customer-employers reduce the wages of their employees who participate in the HealthIER Plan. A sample worksheet entitled "Flexible Savings Estimate" from defendants' training materials shows that the customer-employers using the scheme actually reduce their employees' wages by more than the HealthIER Plan "reimbursements." A copy of the sample worksheet is attached as Exhibit A to this Complaint. The net result is that employees' take-home paychecks are about the same as before using the plan, with most or all of the economic benefits of participating in the bogus scheme going to the employer. Nevertheless the employees earn less in future social security benefits because of the wage understatements. Once the employer's participation in the scheme is detected and unraveled, the employees will be found to owe substantial additional taxes and interest. As a result employees are unwittingly caught up in a fraudulent scheme that exposes them to substantial future expenses.

18. The defendants' customer-employers that use the HI Plan and/or the HealthIER Plan have failed to report and pay substantial amounts of employment taxes. The customers' employees have under-reported and underpaid both FICA taxes and federal income taxes.

19. Defendants promote their schemes through sales agents and on the Internet at [www.PsgWebNet.com](http://www.PsgWebNet.com). On information and belief, defendants also promote a similar scheme to self-employed persons at the site [www.mrp-ssg.com](http://www.mrp-ssg.com).

20. Defendants' promotional materials claim that the accounting firm of Wohlenberg Ritzman & Co. in Yankton, South Dakota, provides "administration" services for the plans. Wohlenberg Ritzman & Co. receives compensation directly from HI Plan or HealthIER Plan fees that defendants' customer-employers withhold from their employees. Blaine Meier, a Certified Public Accountant, and partner with Wohlenberg Ritzman, has written opinions endorsing the HI

Plan and the HealthIER Plan. These opinions do not disclose that Meier or Wohlenberg Ritzman & Co. have a financial interest in the plans. Blaine Meier claims that neither Wohlenberg Ritzman & Co. or the “Processing Center” (which consists of employees of Wohlenberg Ritzman & Co. and which purportedly processes the HealthIER Plan) have access to either a customer list or an employee list.

21. Defendants have sold these fraudulent tax promotions to more than 200 customer-employers.

22. Defendants Zanfei and Crouse have refused to identify to the IRS any of their sales agents or any of their customers. Crouse failed to comply with an IRS summons requiring him to provide documents which identify defendants’ customers. Thus, the IRS cannot identify most of the defendants’ customer-employers, and cannot determine how many employees of the more than 200 customer-employers are affected by the fraud.

23. One customer-employer the IRS has identified is a large medical services provider in California which employs more than 300 people.

24. The IRS estimates that defendants’ schemes have cost the U.S. Treasury losses of \$12 million to \$63 million so far. If defendants are not enjoined, and their scheme dismantled, the United States will lose an additional estimated \$6 million to \$24 million in tax revenue each year. Every paycheck the defendants’ customer-employers pay their employees causes harm to the United States, by understating taxable wages.

#### **Defendants’ False and Fraudulent Statements**

25. Defendants, in connection with these schemes, made statements relating to material matters under the internal revenue laws that they knew or had reason to know were false or fraudulent.

26. Defendants have made the following false and fraudulent statements to their prospective customers:

a. that the prospective customer-employers do not have to pay employment taxes on the amounts paid to employees as so-called medical reimbursement. Because these payments are not reimbursements, this statement is false.

b. that the employees of the prospective customer-employers will not have to pay federal income tax or FICA tax on amounts paid to them as purported medical reimbursements. Because these payments were not reimbursements, this statement is false.

c. that the \$20-per-employee-per-month promoter's fees withheld from employees wages can be excluded from employees' income for federal-income-tax purposes.

**Defendants' Knowledge that the Statements Were False and Fraudulent**

27. Zanfei and Crouse hold themselves out to the public as experts on health reimbursement arrangements. Therefore, they had reason to know about false or fraudulent statements made in connection with their promotion.

28. In April 2001, Stuart Sobel of Stuart Sobel Consulting, Inc., sent a tax opinion on the HI Plan to Zanfei that focused on the HI Plan's purported reimbursement aspects. The



opinion stated that “it was most probable” that the amounts defendants advised their customers to exclude from taxable income under the HI Plan “are includable and not excludible in compensation for healthcare reimbursement.” Defendants nevertheless continued to promote their scheme.

29. Rev. Rul. 2002-3, 2002-3 I.R.B. 316 (January 22, 2002) held that the exclusions from gross income under I.R.C. §§ 106(a) and 105(b) do not apply to amounts that an employer pays to employees to reimburse the employees for amounts paid by the employer for health insurance coverage that are excluded from gross income under IRC § 106(a) (including salary reduction amounts pursuant to a cafeteria plan under I.R.C. § 125 that are applied to pay for such coverage). Defendants Zanfei and Crouse were aware of Rev. Rul. 2002-3 when it was published. Yet they continued to promote their schemes.

30. Rev. Rul. 2002-80, 2002-49 I.R.B. 925 (December 9, 2002) amplified Rev. Rul. 2002-3 to clarify that amounts paid to an employee as advance reimbursements or purported loans without regard to whether the employee has incurred medical expenses are not excludable from the employee’s gross income under IRC § 105(b), that such advance reimbursements or purported loans are included in the employee’s gross income, and that such amounts are subject to employment taxes. Zanfei and Crouse became aware of Rev. Rul. 2002-80 when it was published, yet they continued to promote the HealthIER Plan.

31. Zanfei and Crouse knew of articles published by the Employers Council on Flexible Compensation (ECFC), Employee Benefit Institute of America (EBIA) and other tax professionals that advised that plans like the HI Plan and the HealthIER Plan were unsound.

32. Both the HI Plan promotion and the later HealthIER Plan version of the promotion required prospective customer-employers to sign comprehensive confidentiality agreements to prevent the prospective customer-employers from disclosing information about the promotions to anyone other than the customers' confidential consultants and their employees. Zanfei and Crouse required this in order to keep their fraudulent scheme from being detected.

33. The U.S. Department of Labor sued Zanfei and Crouse, alleging that they violated ERISA when they failed to hold assets of a health plan in trust, failed to charge adequate premiums, and failed to establish appropriate underwriting procedures. As a result, participants were left with between \$5 and \$17.5 million in unpaid medical claims. The suit also alleges that Zanfei and Crouse diverted money targeted to pay health benefits for personal enrichment. *Chao v. Crouse et al.*, Civ. No. 1:03 -cv-01585-DFH-TAB (S.D. Ind.).

#### **An injunction under Section 7408**

34. Section 7408 of IRC authorizes a court to enjoin persons who have engaged in conduct subject to penalty under IRC §§ 6700 or 6701.

35. In relevant part, IRC § 6700 imposes a penalty on any person who organizes (or assists in the organization of) any shelter, plan, or arrangement, or participates (directly or indirectly) in the sale of any interest in an entity or plan or arrangement; and makes or furnishes or causes another person to make or furnish (in connection with such organization or sale) a statement regarding any deduction, credit, or the excludability of income; which the person knows or has reason to know is false or fraudulent as to any material matter.

36. Defendants' conduct as described above is subject to penalty under IRC § 6700.

37. An injunction is necessary and appropriate to stop defendants' conduct subject to the IRC § 6700 penalties and other violations of the internal revenue laws.

38. Defendants are therefore subject to injunction under IRC § 7408.

**Injunction under IRC § 7402**

39. The United States incorporates herein as if fully restated, the allegations in paragraphs 1 through 38.

40. Unless the Court enjoins defendants they are likely to continue to engage in the conduct described in paragraphs 1 through 37 of this complaint.

41. Defendants' conduct described in paragraphs 1 through 37 has resulted and continues to result in irreparable harm to the United States.

42. The United States has no adequate remedy at law to halt this irreparable harm. The United States is entitled to an injunction under IRC § 7402.

43. The United States, as a result of the promotion, has lost and will continue to lose substantial revenues that should have been paid as income tax and employment tax.

44. The detection and audit of customers who have used defendants' scheme, and of those customers' employees, will place serious burdens on the IRS's limited resources.

45. The IRS estimates that 3,000 to 20,000 employees of defendants' customer-employers receive incorrect W-2 wage statements and consequently underreport their state and federal income taxes each year. The task of identifying these employees, examining their income tax returns, determining and assessing deficiencies, collecting unpaid taxes, and correcting Social Security records, is enormous.

46. The customers of defendants, and the employees of their customers, have been harmed financially to the extent they have underpaid their federal tax liabilities and may become liable for additional taxes, penalties and interest, and have paid (and continue to pay) defendants for participation in a fraudulent scheme. Defendants' employees have been further harmed to the extent that underreporting of their wages will lead to reduced social security benefits.

47. If defendants are not enjoined, they likely will continue to engage in unlawful conduct that interferes with the enforcement of the internal revenue laws, thereby undermining the federal tax system.

WHEREFORE, the plaintiff United States prays for the following:

A. That the Court find that the defendants have engaged in conduct subject to penalty under IRC §§ 6700 and 6701, and that injunctive relief is appropriate under IRC § 7408 to prevent them and anyone acting in concert with them from engaging in any further such conduct;

B. That the Court find that the defendants have engaged in conduct that interferes with the enforcement of the internal revenue laws, and that injunctive relief against them and anyone acting in concert with them is appropriate to prevent the recurrence of that conduct, pursuant to the Court's inherent equity powers and IRC § 7402(a);

C. That the Court, pursuant to IRC §§ 7402 and 7408, enter a permanent injunction prohibiting the defendants and their representatives, agents, servants, employees, attorneys, and those persons in concert or participation with them, from directly or indirectly by means of false, deceptive, or misleading commercial speech:

- (1) Organizing, promoting, marketing, or selling (or assisting therein) the Health Incentive Plan, the HealthIER Plan, or any other abusive tax shelter, plan or arrangement that incites taxpayers to attempt to violate the internal

revenue laws, unlawfully evade the assessment or collection of their federal tax liabilities, or unlawfully claim improper tax refunds;

- (2) Further engaging in any conduct subject to penalty under IRC § 6700, *i.e.*, making or furnishing, in connection with the organization or sale of an abusive shelter, plan, or arrangement, a statement they know or have reason to know is false or fraudulent as to any material matter;
- (3) Further engaging in any conduct that unlawfully interferes with the administration and enforcement of the internal revenue laws by the IRS.

D. That this Court, pursuant to IRC §§ 7402 and 7408, enter an injunction requiring the defendants to contact, in writing, by first class mail:

- (1) all persons who purchased the HI Plan, or HealthIER Plan, or any other shelter, plan, or arrangement from the defendants, or from their representatives, agents, servants, employees, attorneys, or other persons acting in concert or participation with them, at any time since January 1, 2000;
- (2) all persons who purchased any shelter, plan, or arrangement at any time since January 1, 2000, from the defendants or any entity (including without limitation any corporation, partnership, limited partnership, limited liability company, proprietorship or other organization or association) in which or with which the defendants have had (a) any ownership interest, (b) any employment relationship, (c) any contractual arrangement, (d) or any other commercial or business affiliation;

- (3) all persons on whose behalf the defendants, or their representatives, agents, servants, employees, attorneys, or other persons acting in concert or participation with them, prepared and/or assisted in the preparation of any federal or state income-tax returns or tax-related documents at any time since January 1, 2000; and
- (4) all persons who contacted the defendants, their representatives, agents, servants, employees, attorneys, or other persons acting in concert or participation with them, regarding the purchase of any shelter, plan or arrangement at any time since January 1, 2000;
- (5) all current and former employees of defendants' customer-employers who at any time since January 1, 2000, participated in the HI Plan or the HealthIER Plan,

and to provide each of those persons with a true, correct and complete copy of the Court's findings and order of permanent injunction, and further, to inform those persons, using a memorandum approved by the Court of the falsity of the representations made by the defendants, of the falsity of any tax returns prepared based on the defendants' plans, of the possibility of the imposition of penalties against them, of the possibility that the United States may seek to recover additional taxes and any erroneous refund they may have received, and of the fact that a permanent injunction has been entered against the defendants.

E. That this Court, pursuant to IRC §§ 7402 and 7408, enter an injunction requiring the defendants to produce to the United States all records in their possession, custody, or control or to which they have access that identify (1) the persons to whom they gave or sold or otherwise provided, directly or indirectly, any documents or other information related to the HI Plan, the

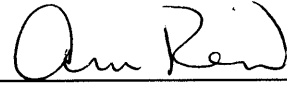
HealthIER Plan, or any other medical reimbursement plan or similar plan or arrangement that the defendants have sold or promoted since January 1, 2000; (2) the persons who assisted in the preparation or marketing of materials used by the defendants or by their representatives, agents, servants, employees, attorneys, or other persons acting in concert or participation with them since January 1, 2000; (3) all individuals or entities for whom the defendants, or their representatives, agents, servants, employees, attorneys, or other persons acting in concert or participation with them, have prepared or have assisted in the preparation of any tax-related documents, including Forms 940, 941, and 5500; and (4) all individuals or entities who purchased or used any other tax shelter, plan, or arrangement with which the defendants have been involved since January 1, 2000.

F. That this Court, pursuant to IRC § 7402, enter an injunction requiring defendants and their representative, agents, servants, employees, attorneys, and those persons in active concert or participation with them, including their distributors, to remove from their websites, including [www.PsgWebNet.com](http://www.PsgWebNet.com) and [www.mrp-ssg.com](http://www.mrp-ssg.com), all abusive tax scheme promotional materials, false commercial speech, and materials designed to incite others imminently to violate the law (including the tax laws), to display prominently on the first page of those websites a complete copy of the Court's permanent injunction, and to maintain the web sites for one year with a complete copy of the Court's permanent injunction so displayed throughout that time;

G. That the Court grant the United States its costs in bringing this action.

H. That the Court grant such other relief as the Court deems appropriate.

PATRICK FITZGERALD  
United States Attorney



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Date Prepared  
9-Mar-2002

Flexible Savings Estimate  
for

**XYZ, Inc.**

**Assumptions:**

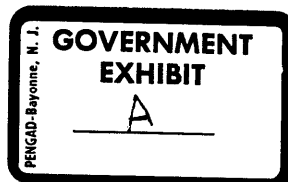
|   |   |             |
|---|---|-------------|
| > | Average Employee Monthly Gross Compensation                           | \$ 2,500.00 |
| > | Average Employer Monthly Contribution to Qualified Benefit Plans*     | \$ 203.33   |
| > | Average Employee Monthly Contribution to Qualified Benefit Plans*     | \$ 21.67    |
| > | Average Number of Employees Participating in Qualified Benefit Plans* | 30          |

| Employee  | Current Plan   |     | HealthIER Plan |
|---|----------------|-----|----------------|
| Monthly Compensation                                      | \$ 2,500.00    |     | \$ 2,500.00    |
| Employee Pre-tax Contribution to Qualified Benefit Plans* | \$ (21.67)     | >>> | \$ (225.00)    |
| HealthIER Plan Administrative Fee                         | Not Applicable |     | \$ (20.00)     |
| Taxable Income for Employee                               | \$ 2,478.33    |     | \$ 2,255.00    |
| Tax Withholdings  |                |     |                |
| Federal Withholding Tax                                   | 15.00%         |     |                |
| State Income Tax  | 3.00%          |     |                |
| Municipal Income Tax                                      | 0.75%          |     |                |
| FICA  | 7.65%          |     |                |
| Net Pay   | \$ 1,824.05    |     | \$ 1,659.68    |
| HealthIER Plan Reimbursement                              | \$ -           | >>> | \$ 165.87      |
| Take-home Pay   | \$ 1,824.05    |     | \$ 1,825.55    |

| Employer                        | Current Plan   |     | HealthIER Plan |
|---------------------------------|----------------|-----|----------------|
| Salary/Wage Expense             | \$ 2,500.00    |     | \$ 2,500.00    |
| Health Insurance Expense        | \$ 203.33      |     | Not Applicable |
| HealthIER Plan Reimbursement    | Not Applicable | >>> | \$ 165.87      |
| Employer FICA Match             | \$ 189.59      |     | \$ 172.51      |
| Total Monthly Cost per Employee | \$ 2,892.93    |     | \$ 2,838.38    |

|  |                     |
|--|---------------------|
| <b>Employer's Estimated Monthly HealthIER Savings per Employee</b> | <b>\$ 54.55</b>     |
| <b>Employer's Estimated Monthly HealthIER Plan Total Savings</b>   | <b>\$ 1,636.35</b>  |
| <b>Employer's Estimated Annual HealthIER Plan Total Savings</b>    | <b>\$ 19,636.20</b> |
| <b>Employer's Daily Cost of Waiting</b>                            | <b>\$ 55.16</b>     |
| <b>Employer's Estimated Minimum Savings Guarantee</b>              | <b>\$ 5,589.38</b>  |

The savings estimated in this illustration have been provided by the Prospect.



This Custom Savings Estimate is not a firm forecast.  
Final calculations per employee will be done during the implementation phase.

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